

**Management Advisory Report:
The Probability of Meeting Electronic Tax
Administration Goals Remains Questionable**

February 2001

Reference Number: 2001-40-047

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

February 16, 2001

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

A handwritten signature in black ink, reading "Pamela J. Gardiner".

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Management Advisory Report – The Probability of Meeting
Electronic Tax Administration Goals Remains Questionable

This management advisory report presents the results of our review of the Electronic Tax Administration (ETA) Strategy. The audit was conducted to determine whether the Internal Revenue Service (IRS) adequately addressed the electronic filing requirements of the IRS Restructuring and Reform Act of 1998 and established appropriate timelines and oversight to ensure these requirements were met. In summary, we found that the IRS has established a framework for accomplishing electronic filing goals in the ETA Strategic Plan, but the probability of meeting these goals remains questionable.

The report identifies opportunities for the agency to improve its strategic planning process. The IRS' ETA budget for Fiscal Year 2000 was over \$100 million. Much of this will be used to implement the 43 projects included in the ETA Strategic Plan. Because several of these projects have implementation schedules spanning multiple years, incremental project milestones and additional performance indicators are needed to measure each initiative's progress and impact on electronic filing.

A formal response was not required to this report. We had requested that if IRS management did choose to respond formally, they do so by February 8, 2001. As of February 12, 2001, the IRS had not responded to this report.

Copies of this report are also being sent to the IRS managers who are affected by the conditions discussed in the body of the report. Please contact me at (202) 622-6510 if you have any questions, or your staff may call Walter E. Arrison, Associate Inspector General for Audit (Wage and Investment Income Programs), at (770) 936-4590.

**Management Advisory Report: The Probability of Meeting
Electronic Tax Administration Goals Remains Questionable**

Table of Contents

Executive Summary.....	Page i
Objective and Scope.....	Page 1
Background	Page 1
Results	Page 3
The Interim Goal for 2003 Will Most Likely Not Be Achieved.	Page 4
Achieving the 2007 Goal Will Require a Significant Increase in the Use of Electronic Filing	Page 4
The Electronic Tax Administration Advisory Committee Played a Significant Role in the Implementation of the Electronic Tax Administration's Strategic Plan.....	Page 10
An Internal Assessment Identified the Need to Better Focus the Electronic Tax Administration Strategy.....	Page 12
Conclusion.....	Page 14
Appendix I – Detailed Objective, Scope, and Methodology	Page 15
Appendix II – Major Contributors to This Report.....	Page 18
Appendix III – Report Distribution List.....	Page 19
Appendix IV – Electronic Tax Administration Total Budget and What the future holds in store for Electronic Tax Administration.....	Page 20
Appendix V – Project Descriptions	Page 22
Appendix VI – Internal Revenue Service e-Services Near Term Release for 2001, e-Services Follow-on Releases for 2002 and Beyond, and Release Descriptions	Page 28
Appendix VII – Implementation Schedules - Individual Income Tax Programs, Other Business Returns Programs and Electronic Payment Programs	Page 32
Appendix VIII – Electronic Tax Administration Advisory Committee Member Organizations 1999/2000	Page 35
Appendix IX – Glossary of Terms.....	Page 36

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

Executive Summary

The Internal Revenue Service (IRS) processes over 200 million returns while collecting tax revenues totaling \$1.7 trillion each year. Although such figures make the IRS the largest processor of tax data in the world, efforts to modernize its processing systems remain constrained since most tax returns are filed on paper rather than electronically using a computer.

The United States Congress recognized the importance of electronic filing in the IRS Restructuring and Reform Act of 1998 (RRA 98).¹ Two important requirements of this legislation include a long-range goal to have 80 percent of all federal tax and information returns filed electronically by 2007 and to have all paper returns that are prepared using a computer filed electronically by 2003. Increasing electronic filing improves tax return processing by significantly reducing errors and labor costs and is essential for modernization to be effective.

The IRS' Electronic Tax Administration (ETA) budget for Fiscal Year 2000 was over \$100 million. Much of this was used to implement the 1999 ETA Strategic Plan, *A Strategy for Growth*, which described how the IRS plans to achieve its electronic filing goals. To independently assess results derived from the strategic plan, the Congress required the IRS to establish the Electronic Tax Administration Advisory Committee (ETAAC) to periodically report on electronic filing progress. Committee members are comprised of non-federal government employees selected from various private sector communities.

This audit was conducted to determine whether the IRS adequately addressed the electronic filing requirements of the RRA 98 and established appropriate timelines and oversight to ensure these requirements were met.

Results

The IRS established a framework for accomplishing its electronic filing goals in the ETA Strategic Plan, but the probability of meeting these goals remains questionable. From 1998 to 1999, the IRS increased the number of electronically filed returns over 19 percent for individual returns and 56 percent for information returns. During 2000, it also experienced an increase in electronic filing. For example, electronically filed individual returns increased from 23.4 percent in 1999 to 28 percent in 2000.

¹ Pub. L. No. 105-206, 112 Stat. 685.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

While this is a noteworthy accomplishment, achieving the RRA 98 interim goal to have all returns prepared using a computer to also be filed electronically by 2003 is not probable. It is also questionable whether the IRS can accomplish the RRA 98 goal to have 80 percent of all tax returns filed electronically by 2007. To succeed will require a sustained and substantial effort by the IRS to increase the number of electronically filed returns over the next 7 years.

Percentage of E-filed Returns for 1999 (In Millions)

	Total	E-file	% of Total
Individual Returns	125.1	29.3	23.4
Business Returns	69.8	5.7	8.2
Information Returns	1,240.0	121.5	9.8
Total	1,434.9	156.5	10.9

Source: ETA Strategy for Growth, Information Return Volumes for 1999 from the Executive Officer of Service Center Operations, and Statistics of Income Projections for Returns to be Filed

The IRS should improve its strategic planning process. Its ETA Strategic Plan communicated the ETA mission, goals and strategies, market opportunities, and challenges for growth. It also included 43 projects, many with implementation schedules spanning multiple years. However, the plan did not include incremental project milestones or sufficient performance measures to evaluate each initiative's progress or its ultimate impact on electronic filing.

The ETA Strategic Plan should also clearly define the impact of information returns filed on magnetic media. These returns will significantly affect the IRS' ability to achieve its electronic filing goals because banks and employers will need to convert over one billion returns from magnetic tape to electronic filing within the next 7 years. The plan did not adequately distinguish between those returns filed electronically versus those received on magnetic tape.

In January 2000, the IRS reviewed the ETA strategy and identified the need to focus its efforts on the most critical issues. In addition, the IRS received meaningful feedback from the ETAAC. The ETAAC's June 2000 report emphasized that the past increases in the electronic filing rate must be sustained and suggested establishing new initiatives to help achieve the growth rate necessary to accomplish ETA filing goals in future years. By addressing these concerns and implementing enhancements in the strategic planning process, the IRS should increase the likelihood that its vision for electronic filing becomes a reality.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

Objective and Scope

The overall objective of the audit was to determine whether the IRS established appropriate timelines and oversight to ensure RRA 98 electronic filing requirements were met.

This review supports our Fiscal Year (FY) 2000 emphasis area to address major management issues facing the Internal Revenue Service (IRS).

The overall objective of the audit was to determine whether the IRS adequately addressed the electronic filing requirements of the IRS Restructuring and Reform Act of 1998 (RRA 98)¹ and established appropriate timelines and oversight to ensure these requirements were met. To accomplish this objective, we reviewed the IRS' 2003 and 2007 electronic filing goals and determined whether these goals were adequately defined and structured to accurately measure and report results.

We performed audit work at the Electronic Tax Administration (ETA) headquarters located in Washington, D.C., in May and June 2000. The supporting audit work was executed in compliance with the *President's Council on Integrity and Efficiency's Quality Standards for Inspection*.

Details of our audit objective, scope, and methodology are presented in Appendix I. Major contributors to this report are listed in Appendix II.

Background

Reducing the volume of paper returns to be processed is a key issue in the modernization of the IRS.

The IRS processes over 200 million returns while collecting tax revenues of \$1.7 trillion each year. Although such figures make the IRS the largest processor of tax data in the world, efforts to modernize its processing systems remain constrained since most tax returns are filed on paper rather than electronically using a computer.

¹ Pub. L. No. 105-206, 112 Stat. 685.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

	<p>Broadening the use of electronic filing is a key component of the IRS' modernization efforts. Electronically filed returns improve taxpayer service and increase production by reducing errors, accelerating refunds, and decreasing labor costs.</p>
<p><i>The Congress enacted legislation to emphasize and provide goals for electronic filing.</i></p>	<p>The United States Congress recognized the importance of electronic filing in the RRA 98. Two important requirements of this legislation included a long-range goal to have 80 percent of all federal tax and information returns filed electronically by 2007 and to have all paper returns that are prepared using a computer filed electronically by 2003.</p>
<p><i>The IRS has developed a strategic plan for electronic filing and invested a great deal of resources in accomplishing this plan.</i></p>	<p>The ETA budget for FY 2000 was over \$100 million. Much of this was used to implement the 1999 ETA Strategic Plan, <i>A Strategy for Growth</i>, which described how the IRS plans to achieve electronic filing goals. The plan communicated the ETA mission, goals and strategies, market opportunities, and challenges for growth. It also contained more detailed information in appendices containing the Products and Services, the Evaluation Methodology used for ETA initiatives, the Business Goals, an Industry Overview, and IRS E-file Projections.</p> <p>To independently assess results derived from the ETA Strategic Plan, the Congress required that the IRS establish the Electronic Tax Administration Advisory Committee (ETAAC) to annually report on electronic filing progress. Committee members are comprised of non-federal government employees selected from various private sector communities.</p>
<p><i>The GPRA has defined what elements should be included in a strategic plan.</i></p>	<p>As defined by the Government Performance and Results Act of 1993 (GPRA),² a strategic plan³ should contain:</p> <ul style="list-style-type: none">• General goals and objectives with the goals defined in a method that allows for a future assessment to be made on whether or not they were achieved.

² Pub. L. No. 103-62, 107 Stat. 285.

³ Office of Management and Budget Circular No. A-11 (1998).

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

Performance goals that represent milestones in achieving goals of the strategic plan may be appropriate.

- The processes, skills, technologies, and other resources that will be used to achieve the general goals and objectives.
- Schedules for initiating or completing significant actions (and any assumptions or projections).
- The type, nature, and scope of performance goals. Performance goals that represent milestones in achieving the general goals and objectives of a strategic plan may be appropriate.
- Key factors external to the agency that could significantly affect achievement of the goals.
- A schedule for program evaluations, including the methodology to be used.

Results

The IRS established a framework for accomplishing electronic filing goals in its ETA Strategic Plan, but the probability of meeting these goals remains questionable. It is very unlikely that the interim goal for 2003 will be met. In addition, significant steady growth must be sustained for the 2007 goal to be feasible.

The IRS needs to improve its strategic planning for ETA to improve its likelihood of achieving its goals.

Improvements in strategic planning are needed to assist the IRS in identifying problems or weaknesses that may affect its ability to meet the requirements of the RRA 98. The ETA Strategic Plan does not provide adequate details of interim goals or performance indicators to effectively measure the IRS' progress towards electronic filing goals.

A recent internal review by the IRS identified the need to focus efforts on the most critical ETA issues. In addition, the IRS received meaningful feedback from the ETAAC. By addressing these concerns and implementing enhancements in the strategic planning process, the IRS should increase the likelihood that its vision for electronic filing becomes a reality.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

The Interim Goal for 2003 Will Most Likely Not Be Achieved

Both the IRS and the ETAAC believe that the 2003 goal is unlikely to be met.

The ETAAC and the Council for Electronic Revenue Communication Advancement, Inc., (CERCA) recommended that the IRS modify its 1999 ETA Strategic Plan to include the 2003 intermediate goal in order to establish a yardstick for determining whether the IRS is on track. This goal requires that virtually 100 percent of all tax returns prepared using a computer should also be filed electronically by 2003.

The IRS realizes that achieving this goal is unlikely since taxpayers that prepare their returns using a computer are not authorized to electronically file them with the IRS. If they choose to file electronically, they must file through an authorized Electronic Return Originator (ERO) that generally charges a fee for this service. In its June 30, 2000, report to the Congress, the ETAAC projected that the IRS' goal for 2003 would not be achieved.

During the 2000 Filing Season, the IRS estimated that approximately 80 million (62 percent) of individual tax returns were prepared using a computer but filed in a paper format. These tax returns contained a three-character software code in the bottom margin of the document. The IRS identified these returns during processing to evaluate its progress in meeting this goal.

Achieving the 2007 Goal Will Require a Significant Increase in the Use of Electronic Filing

Achieving 80 percent electronic filing in each group of returns will be difficult and will require sustained significant increases each year.

The IRS interpreted the RRA 98 goal to mean 80 percent of individual, business, and information returns as applied to each group rather than to all return groups combined as one. While the IRS has experienced a significant increase in the number of electronically filed returns, much more progress is

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

needed. The following chart shows the IRS' 1999 electronic filing rate for each of these groups.

**Percentage of E-filed Returns for 1999
(In Millions)**

	Total	E-file	% of Total
Individual Returns	125.1	29.3	23.4
Business Returns	69.8	5.7	8.2
Information Returns	1,240.0	121.5	9.8
Total	1,434.9	156.5	10.9

Source: ETA Strategy for Growth, Information Return Volumes for 1999 from the Executive Officer of Service Center Operations, and Statistics of Income Projections for Returns to be Filed

From 1998 to 1999, the IRS increased the number of electronically filed returns over 19 percent for individual returns and 56 percent for information returns. During 2000, electronically filed returns continued to increase. For example, the number of electronically filed individual returns increased from 23.4 percent in 1999 to 28 percent in 2000. Electronically filed information returns also increased from 14.7 percent filed in the first five months of 1999 to 18.5 percent filed during the same period in 2000.

To meet the 80 percent goal, the IRS must sustain increase rates per year of 19 percent for individual returns and 35 percent for information returns.

However, to achieve the 80 percent goal, the IRS must significantly increase the use of electronic filing over the next 7 years. Specifically, based on our projections, the IRS will need to increase electronic filing by an average of 19 percent per year for individual tax returns (29.3 million in 1999 to 110.9 million in 2007). In addition, electronically filed information returns will need to increase 35 percent per year (121.5 million in 1999 to 1,345 million in 2007). The expected growth rate of total returns and needed growth rates of electronic returns are shown separately for individual and information returns in the following charts.

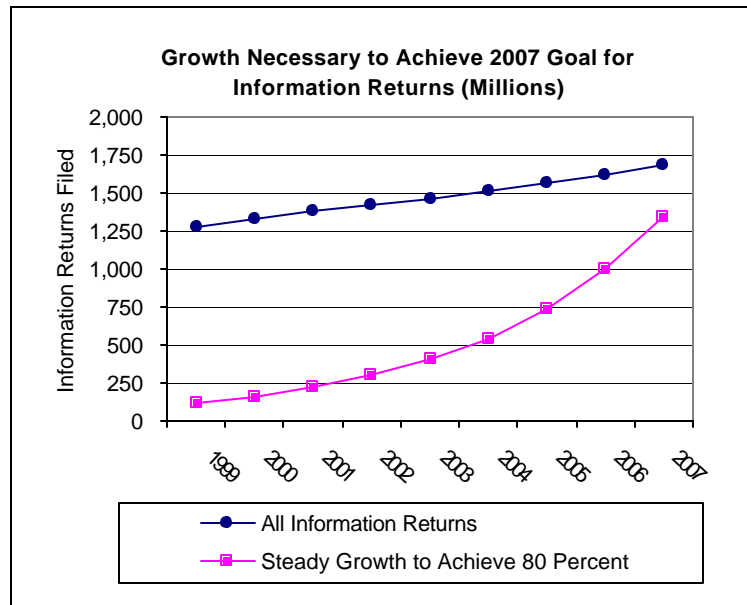
Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

Significantly affecting these efforts for information returns is the magnetic tape issue. The conversion of information returns from magnetic tape to electronic filing will require banks and employers to convert over one billion returns within the next 7 years.



Source: 1999 A Strategy for Growth and the ETACC Report to Congress dated June 30, 2000.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable



Source: Statistics of Income Projections of Information and Withholding Documents in the United States for Paper and Non-Paper Totals for Filing Seasons 2000-2008 and Combined Total of Electronically Transmitted Magnetic Tape and Paper

The impact of information returns filed on magnetic tape should be clearly defined

The IRS does not consider the use of magnetic tape to be electronically filed.

The large number of information returns that are filed on magnetic tape significantly affects whether the IRS' electronic filing goals are met, since the IRS does not consider the use of magnetic tape to be electronically filed. The ETA Strategic Plan does not clearly address this issue. For example, the Strategic Plan:

- Does not make the distinction between information returns filed electronically versus those filed on magnetic tape.
- Includes projections for information returns that will still be received on magnetic tape in 2007.
- Includes one project currently in the development phase that will receive information returns both electronically and on magnetic tape in 2007.

The IRS agreed the magnetic tape classification could be misleading.

The IRS indicated that the classification of magnetic tape as non-electronic data could be misleading and plans to

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

address and clarify its classification when the ETA’s Strategic Plan is updated for 2000.

Additional performance measures are needed

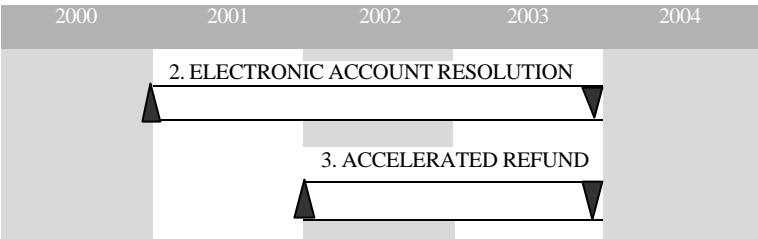
As previously discussed, the IRS’ ETA budget for FY 2000 totaled over \$100 million and helped fund various evolving filing initiatives that could create an increase in electronic filing in the future. (The breakdown of the ETA budget and a detailed description of these initiatives are included in Appendix IV.)

The ETA Strategic Plan included 43 specific projects and initiatives. (Detailed project descriptions are included in Appendix V.) The Strategic Plan stated that, “these initiatives were derived from a variety of sources and screened by the IRS to limit the plan to those initiatives that could be accomplished by 2004 and were directly tied to strategic goals or known mandates.”

The IRS reported that its methodology for selecting these projects included criteria for business requirements, business risks, technical risks, stakeholder risks, and level of effort. While we did not conduct a detailed analysis of this selection process, the methodology as described by the IRS appears to be sound.

The Strategic Plan contains many projects with implementation schedules that span several years but do not have interim goals or measures to help determine progress.

The Strategic Plan also contained project implementation schedules as shown in the table below.



Many projects have implementation schedules spanning several years. However, they do not have interim milestone dates or performance measures that allow the IRS to measure the projects’ progress or forecast their impact on electronic filing.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

For example, the e-Services Project is intended to accelerate the IRS' efforts to update its business systems so ETA can provide e-Services that are comparable to private industry and meet the expectations of taxpayers, tax preparers, and the Congress. The 2001 release will provide services primarily to tax preparers and their customers. The IRS e-Services Project Description for the 2002-2007 strategic releases indicated that it would build on the business systems delivered in 2001 and focus more resources on business customers. The e-Services Project did not contain any milestone dates or performance indicators to measure the progress during the 6 years of implementation. (Appendix VI includes charts of the e-Services Near Term Release for 2001 and the Follow-on Releases for 2002 and Beyond and Appendix VII includes the implementation schedule of the 43 projects with no incremental milestone dates.)

In conclusion, the 1999 ETA Strategic Plan, *A Strategy for Growth*, showed calendar year projections indicating the IRS will not make its 2007 goal.

Calendar Year Projections indicate the IRS will not make the 2007 goal.

**Calendar Year Projections of the Percentage of
Individual Returns to be Filed Electronically
2000-2007 for the United States
(In Millions)**

Year	Total Individual Returns	Total e-file Returns	e-file Percent of Total
1998 Actual	122.5	24.6	20.1
1999 Estimated	125.1	29.3	23.4
2000	126.9	33.6	26.5
2001	129.1	38.0 - 41.4	29.5 - 32.1
2002	130.7	41.2 - 45.6	31.5 - 34.9
2003	132.1	44.1 - 49.4	33.4 - 37.4
2004	133.5	46.8 - 52.9	35.1 - 39.7
2005	135.1	49.6 - 56.6	36.8 - 41.9
2006	136.9	52.5 - 60.4	38.4 - 44.1
2007	138.6	55.5 - 64.3	40.0 - 46.4

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

The Electronic Tax Administration Advisory Committee Played a Significant Role in the Implementation of the Electronic Tax Administration's Strategic Plan

The ETAAC is an advisory group that insures the IRS receives input from the private sector regarding the implementation of the ETA Strategic Plan to encourage electronic filing.

The ETAAC is required to make an annual report to the Congress on the progress the IRS is making in meeting the 80 percent goal by 2007.

As required by the RRA 98, ETAAC members for 1999/2000 included 22 representatives from large and small tax practitioners, service organizations, academia, tax return software companies, state tax representatives, and banking and investment services.⁴ (Appendix VIII includes a list of the organizations represented on the ETAAC.)

The ETAAC chair, along with the IRS Oversight Board chair, and the Secretary of the Treasury are required to make an annual report to the Congress no later than June 30th of every year after 1998. This report must include the IRS' progress in meeting the goal of receiving 80 percent of tax and information returns electronically by 2007. The progress of the Strategic Plan and legislative changes necessary to assist the IRS in meeting its goal must also be reported.

The ETAAC issued its first report on June 30, 1999. That report included 52 recommendations in various areas. Some of these recommendations were:

- Ensure all initiatives identified in the Strategic Plan are incorporated within overall IRS strategic planning efforts.
- Apply the necessary resources to accomplish the initiatives described in the Strategic Plan and create and implement an integrated strategic plan.
- Develop a strategy to encourage every professional tax practitioner to file electronically.
- Implement a strategic management process that is based on continual progress evaluation against

⁴ We did not analyze the selection process for the ETAAC members.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

established milestones, with provision for identifying new projects and corrective action.

- Make electronic tax administration initiatives a high priority in the IRS' Information Technology modernization so they are synchronized with major IRS modernization blueprints rather than competing for attention in later years.

The IRS increased emphasis in some of these areas in its 1999 ETA Strategic Plan, *A Strategy for Growth*. In response to these recommendations, the IRS also created an ETAAC Strategic Plan Recommendations listing that included all the recommendations, the responsible offices for actions, and the completion dates. The IRS advised us that many of these recommendations were too broad to adequately accomplish, and it discussed making more focused recommendations with the ETAAC. This was accomplished by the ETAAC in its June 30, 2000 report.

The ETAAC concluded the IRS will not achieve the 2003 goal and identified five critical challenges the IRS must overcome to meet its goals.

The June 2000 report stated that while progress had been made, much work remained to be done. It also concluded that the IRS would not achieve its 2003 goal and that the 2007 goal can only be achieved if a growth rate of 19 percent or better is maintained. The ETAAC believes that new initiatives will be needed to maintain the growth rate at this level and recommended that the IRS closely monitor the total growth rate for electronic filing in future years.

The ETAAC identified five critical challenges the IRS must overcome to meet its goals. They are:

1. Continuing to develop a strategic planning process to achieve goals.
2. Encouraging all professional tax preparers to be EROs and convincing them that filing and communicating with the IRS electronically is preferable to other methods.
3. Increasing electronic filing among self-preparers to at least 70 percent.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

4. Increasing electronic interactions between the IRS and businesses, including filing, paying, and communicating activities.
5. Forming strategic alliances with businesses, federal government agencies, states, and other organizations to facilitate and promote the growth of electronic tax administration.

An Internal Assessment Identified the Need to Better Focus the Electronic Tax Administration Strategy

The IRS reviewed the ETA strategy and identified five other key problems that stand in the way of meeting the ETA goals.

At the completion of our review, we received an assessment of the ETA strategy performed by the IRS in January 2000. This review concluded that a sharper focus and clearer commitment were needed to solve a few key problems that stand in the way of meeting the goals for ETA and the RRA 98. These problems included the following:

1. Expanding electronic filing to include tax returns requiring complex tax schedules that have not been programmed for electronic processing. In addition, unlike electronic filing, tax practitioners can attach notes and comments as part of a paper return package mailed to the IRS. A clear solution to this problem needs to be addressed so the practitioners can file their returns electronically.
2. Finding an alternative to the legal statute that requires electronic filers to also file a paper “jurat” as a means of signature authentication. This requirement creates an additional burden for taxpayers choosing to file electronically. Personal Identification Number pilots are underway, but are limited to specific taxpayers. There are no clear plans or deadlines on *how* and *when* all electronic 1040 filers will be able to eliminate the separate paper form.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

3. Developing and improving methods for taxpayers to electronically pay as well as electronically file a tax return showing a balance due amount. Focus group or market testing needs to be done to determine if proposed debit and credit card methods will be convenient and acceptable to balance-due taxpayers. In addition, options need to be developed to reduce the cost to the taxpayer for using the credit card option.
4. Eliminating or minimizing the taxpayer out-of-pocket cost that is currently associated with electronic filing. The IRS does not yet have a beneficial plan to solve this problem.
5. Identifying the total costs necessary to implement electronic filing and determining how these costs can be minimized to meet the requirements of the IRS' new organizational structure.

A high-level group with a separate team for each issue was assembled to address problems and come to clear conclusions on solving them.

The IRS appointed a high-level group to address these problems and come to clear conclusions on solving them. This high-level group formed five teams with a team leader to address each of these key problem areas and report on them. One key problem area, the IRS cost of processing, was not included in the *Resolving Impediments to E-Filing* report because current and future electronic filing cost projections to the IRS were not analyzed.

The remaining four teams addressed four key questions and identified the analysis required. They identified options, along with descriptions of the options, and used the following evaluation criteria for these options:

- Investment cost to the IRS to implement option.
- Implementation risk to the IRS to set up and implement option.
- Infrastructure impact with additional demands placed on the IRS infrastructure across all areas resulting from implementation and use of option.
- E-file impact in the increase in the number of potential E-filers.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

- ETA drivers:
 - Congressional mandated RRA 98 e-filing goals.
 - Directive that the IRS' top priority is "to eliminate as many 1040 paper returns as possible."
 - IRS cost management by using the increase of e-filing to hold if not lower overall operating costs.

The high-level group issued its report and recommendations on April 10, 2000.

The teams then made a recommendation of an option based on this analysis. This report, *Resolving Impediments to E-Filing*, was issued on April 10, 2000.

Conclusion

The IRS' current planning efforts need improvement if the IRS is to accomplish its electronic filing goals.

The IRS has established a framework for accomplishing its electronic tax administration goals within its ETA Strategic Plan. However, the probability of meeting these goals remains questionable. To provide a greater assurance that the IRS will accomplish these goals, it should further refine its strategic planning process.

Detailed Objective, Scope, and Methodology

The overall audit objective was to determine whether the Internal Revenue Service (IRS) adequately addressed the electronic filing requirements of the Internal Revenue Service Restructuring and Reform Act (RRA 98)¹ and established appropriate timelines and oversight to ensure that these requirements were met. The following steps were completed to accomplish the audit objective:

- I. Reviewed the IRS' goal of having all returns prepared electronically also be filed electronically by 2003 and determined whether this goal was adequately defined and structured to effectively measure and report results.
 - A. Reviewed the progress of this goal and determined what actions were being taken by Electronic Tax Administration (ETA) management to ensure the goal was on schedule.
 - 1. Interviewed ETA management to determine what actions were being taken to ensure this goal was met and if they believed this goal was realistic.
 - 2. Reviewed how ETA identifies the volume of returns that is electronically prepared but submitted in a paper format to determine if the data were reliable.
 - 3. Identified from ETA management if problems encountered or anticipated would impact meeting this goal.
 - 4. Identified any significant changes or issues that had occurred since the release of the December 1999 ETA Strategic Plan and determined if these changes had been reported.
 - B. Reviewed ETA timelines and program reports to substantiate whether significant milestones were realistic and designed to be effectively monitored for timely implementation.
 - 1. Determined whether critical milestones had been reached.
 - 2. Obtained available ETA filing statistics and determined if the ETA strategy projections were revised based on these statistics.

¹ Pub. L. No. 105-206, 112 Stat. 685.

Management Advisory Report: The Probability of Meeting Electronic Tax Administration Goals Remains Questionable

3. Reviewed an assessment of the strategy performed by the IRS in January 2000 that identified five critical problem areas in need of clear plans to resolve.
- II. Reviewed the IRS' goal of having 80 percent of all tax and information returns filed electronically by 2007 and determined whether this goal was adequately defined and structured to effectively measure and report results.
- A. Reviewed the progress of this goal and determined what actions were being taken by ETA management to ensure the goal was on schedule.
 1. Interviewed ETA management to determine what actions were being taken to ensure this goal was met and if they believed this goal was realistic.
 2. Determined if problems had been encountered or anticipated that would affect meeting this goal.
 3. Identified any significant changes or issues that had occurred since the release of the December 1999 ETA Strategic Plan and determined if these changes had been reported.
 - B. Identified whether an ETA strategic planning process had been established to support this goal. In addition, we determined if this process ensured that selected ETA projects were evaluated for their return on investment potential and if the results of this evaluation were analyzed to identify if the potential was realized. Ensured the ETA strategic planning process included:
 1. A strategic plan that was integrated with the IRS' planning and budgeting processes.
 2. An intermediate goal for 2003 consistent with the IRS' Balanced Measurement System.
 3. A vision statement.
 4. A schedule for products and services that refined and identified ETA modernization releases.
 5. Revised projections of IRS E-file returns.
 - C. Reviewed how the determination was made to interpret the law differently than it was written.
 1. Determined how ETA was defining electronically-transmitted returns for reporting purposes.
 2. Identified how magnetic tape was classified for achieving electronic volumes.

**Management Advisory Report: The Probability of Meeting
Electronic Tax Administration Goals Remains Questionable**

- D. Determined if balanced measures had been adequately defined and implemented to measure customer satisfaction. Reviewed ETA performance measures to determine whether they indicated the progress ETA was making towards its goal.
- E. Determined if the Electronic Tax Administration Advisory Committee, the Council for Electronic Revenue Communication Advancement, Inc., the Federation of Tax Administrators, and the Service Bureau Consortium recommendations were tracked and valid issues were incorporated in updates to the ETA Strategic Plan.

Major Contributors to This Report

Walter E. Arrison, Associate Inspector General for Audit (Wage and Investment Income Programs)

M. Susan Boehmer, Director

Gary L. Young, Audit Manager

Tina M. Parmer, Senior Auditor

George E. Millard, Auditor

John P. Ojeda, Auditor

**Management Advisory Report: The Probability of Meeting
Electronic Tax Administration Goals Remains Questionable**

Appendix III

Report Distribution List

Commissioner, Wage and Investment Division W
Director, Electronic Tax Administration W:E
Director, Legislative Affairs CL:LA
National Taxpayer Advocate TA
Office of Management Controls N:CFO:F:M
Office of the Chief Counsel CC
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O
Audit Liaison: Director, Electronic Tax Administration W:E

Please note that Appendices IV and V are included in a separate Adobe PDF file Part 2. Appendices VI through IX are in the Adobe PDF file Part 3. These appendices were placed in separate files due to their size.